Will Open Banking increase competition? I think not.

There is a disconnect between the Commerce Commission's definition of the problem and the recommended solution. Yes, there is a problem with switching banks, but Open Banking, no matter how useful it is in other ways, will not resolve that problem.

The Problem – Bank Stickiness

The Commerce Commission identified "barriers to consumer switching and engagement" as one of four main factors limiting competition. The analysis method employed appears to be survey rather than developing an understanding of the intricacies of the banking system that create stickiness. I attempt this latter approach to develop a pragmatic and holistic view of the issues.

It seems relatively clear that there are three main barriers to changing bank:

1. the complexity of opening an account (including identifying yourself)
2. the complexity of transferring payment relationships
3. the cost and complexity of moving mortgages and investments

Account opening will always be required and can be complex. The challenge of providing an identity is particularly onerous at times, especially if an account has multiple owners.

Transferring payments is especially challenging. NZ banking lacks any central control of payees. Customers have established different payment options at different times over the last few decades (bill payment, automatic payments, direct credit, credit card). With no central point and variable processes, it is a daunting task to simply know what payments are set up, let alone actually reconfigure these payments to point to another bank.

Obviously mortgages and investments are problematic due to the cost of changing an agreed contract and the legal costs associated to execute any change.

For a customer switching banks, the obvious process would be to open an account and switch payments relationships, leaving investments and mortgages to run out or be transferred in a timely manner.

While it would be ideal to approach all three issues, it would be pragmatic to approach account opening and transferring payment relationships first, as the mortgage and investment issue is a highly complex mix of technology, standards, and commercial issues.

To do so, the Commerce Commission should ask "What industry solutions are required to make account opening and payment relationship transfers easier for customers?"

Open Banking

At the recent Commerce Commission conference, there was a lot of positive discussion about Open Banking especially from the major banks. But the question is "will Open Banking in NZ substantially increase retail banking competition?" And to answer that question requires an understanding of Open Banking.

Open Banking is many things:

1. **A nebulous concept** that can mean almost anything! This is partly the reason I am writing this document.

2. **A regulatory approach.** This refers primarily to the EU and the PSD2 laws that regulates the establishment of secure environments for innovation payments and Open Banking. They are an important as they establish the conditions for innovation to be possible.

3. **Banking industry API centres.** This is what the UK have regulated, and what NZ has achieved, without regulation, through Payments NZ's API Centre. Both versions stipulate customer-controlled access to account information and payment services. Both will enable fintech innovation to deliver new services. And in NZ, it has not been easy, and the industry is to be congratulated.

4. **An approach to building a bank.** Two neobanks in the UK are Monzo and Starling. They both are digital banks that have reputedly changed the UK competitive landscape. And they were both formed BEFORE Open Banking was even announced in the UK! It can be argued that they were ahead of their time, and they contributed to the formation of Open Banking, but they are still both banks with large capital bases. They are not fintechs.

In NZ, Open Banking is the Payments NZ API centre. This has and will enable innovation on the edges of the banking system by fintechs. It will not influence the establishment of any neobanks.

In one areas, payments, it may enable fintech real-time payment solutions to be implemented in niche markets. But, it will not drastically change the payments landscape. It will also enable umbrella banking services but these have been tried and failed previously, and it will support other lenders accessing transaction histories for credit checks, but this, while useful, is not transformational.

Given these limited applications, Open Banking will not significantly change the overall retail banking competitive landscape.

How reduced stickiness could increase competition

Barriers to consumer switching is rightly identified as a major factor in reduced competition. But the Commerce Commission does not make it clear if the competition envisaged is between the current major banks or a new entrant.

In the current oligopoly situation, with well established patterns of behaviour, it may well be that reducing customer stickiness will not have much effect. If customers simply switch between the current majors, little is achieved.

The aim of reducing stickiness should be to attract a new low-cost, high-service bank to NZ. This could be a so-called neobank. It is such a large move that is required to significantly enhance competition.

Summary

Reducing barriers to consumer switching is a valid and necessary development if competition is to be improved. Open Banking will not significantly contribute to it. Presenting Open Banking as the answer gives the illusions of progress happening and removes any focus from the real issue at hand, that being improving consumer switching.

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